

ORIGINAL

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FEDERAL COMMUNICATIONS COMMISSION  
OFFICE OF THE SECRETARY

Ms. Magalie R. Salas  
Secretary  
Federal Communications Commission  
445 12<sup>th</sup> Street, SW, Room TW-A325  
Washington, DC 20054


Re: CC Dkt. 00-199/2000 Biennial Regulatory Review—Comprehensive  
Review of Accounting Requirements

Dear Ms. Salas,

On September 6, the undersigned, Lyn Rogers-Haney, and Steve Earnest of BellSouth, met in separate meetings with Kyle Dixon of Chairman Powell's office and Sam Feder of Commissioner Martin's office. The purpose of the meetings was to discuss proposals in the above referenced docket regarding streamlining affiliate transactions rules. Material used during the meetings is attached.

This notice is being filed pursuant to Sec. 1.1206(b)(2) of the Commission's rules. If you have any questions concerning this filing, please do not hesitate to contact me.

Sincerely,

  
Mary L. Henze

cc: K. Dixon  
S. Feder

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List A B C D E

## Affiliate Transaction Rules: Time for Change

### Original Purpose of Rules No Longer Valid

- ❑ FCC's affiliate transactions rules were "designed to keep incumbent local exchange carriers from imposing the costs and risks of their competitive ventures on interstate telephone ratepayers."
- ❑ A valid purpose when telephone company costs had direct impact on ratepayer rates, and misallocation of costs could justifiably be considered a "risk."
- ❑ "Risk" is gone due to recent regulatory actions:
  - current price cap plan with no sharing
  - removal of LFAM through pricing flexibility
  - reliance on forward-looking UNE pricing
- ❑ FCC recognized in 1993 that adoption of price caps for AT&T eliminated the "risk" associated with affiliate transactions. Under price caps, affiliate transactions have no impact on rates.\*
- ❑ It's time to recognize the same is true for price cap ILECs; rules are no longer valid.

\*FCC recognized in 93-251 "Since the adoption of the affiliate transactions rules, we have adopted a price cap system for AT&T that imposes no sharing obligations. This system greatly reduces the incentives that AT&T may have to shift costs between its nonregulated operations and its carrier operations. Since AT&T's price caps are unrelated to AT&T's current costs, attempts by AT&T to manipulate the costs it records for affiliate transactions will not increase AT&T's rates."

## **Current Rules are Costly and Not Competitively Neutral**

- ❑ Under current rules, transactions between regulated company and affiliates must be valued at publicly available rates or on an asymmetrical “comparison of fully distributed cost and fair market value.”
  - FDC/EFMV comparison is be costly and drives inefficient business practices that benefit no one.
- ❑ In addition, asymmetrical rules are not competitively neutral.
  - Designed to provide an advantage to ILEC regulated operations by requiring booked amount at “lowest” level.
  - No longer appropriate in competitive local market.

## **FCC Action Needed**

- ❑ Entire asymmetrical FDC/EFMV comparison structure should be removed. FCC could do so immediately without risk.
- ❑ At minimum, all the affiliate transactions proposals presented by BellSouth/USTA in Phase 2 proceeding should be adopted.
  - Proposals are designed to reduce burden of FDC/EFMV comparison
  - Must be adopted as proposed to achieve streamlining goals

## Specific BellSouth/USTA Proposals

### **1. Redefine FDC/EFMV Exemption for Centralized Services**

*Issue:* Current exemption applies only when entire legal entity provides 100% of all services to corporate family. A single sale of a single service outside the corporate family, triggers EFMV/FDC comparison for all other transactions of that affiliate, even if they are provided 100% within corporate family.

*Solution:* Service exemption should apply on a service-by-service basis instead of being applied to an entire legal entity. By applying exemption to any individual service that is provided 100% within the corporate family, relevant transactions will continue to be subject to EFMV/FDC comparison without burdening other services unnecessarily. (See Attachment A1 and A2)

### **2. Establish FDC/EFMV Threshold for Asset Transfers on Affiliate-by-Affiliate Basis**

*Issue:* The FCC's proposed \$500,000 threshold would provide NO reduction in burden because it would apply on a product-by-product basis for the total amount of transfers for a given product line in a given year.

*Solution:* As proposed by BLS/USTA, threshold would apply on a product-by-product, affiliate-by-affiliate basis and would provide significant reduction in burden. (See Attachment B).

### **3. Correct Threshold Adopted for Service Transactions in Phase 1 to Apply on Affiliate-by-Affiliate Basis**

*Issue:* Threshold for service transactions as adopted by FCC in Phase 1, provides little to NO reduction in burden because it applies to "total aggregate annual value of service."

*Solution:* As proposed by USTA in Phase 2, modify threshold to apply on affiliate-by-affiliate basis (i.e., "annual value of service transferred between two individual affiliates.")

### **4. Exempt Nonregulated to Nonregulated Transactions from Affiliate Transactions Rules**

*Issue:* Transactions between the regulated entity and one of its non-regulated affiliates involving a non-regulated service are now subject to FDC/EFMV comparison.

*Solution:* Such transactions should be exempt from comparison. All costs for these non-regulated services are already properly allocated pursuant to reg/non-reg cost-allocation rules. Any non-regulated service also sold to third parties should simply be recorded at market rates. If provided solely to BellSouth affiliates, should be treated as a service exemption (see Item 1, above)

### **5. Decrease Prevailing Price Threshold from 50 percent to 25 percent.**

*Issue:* Current rule requires affiliate to have external sales of 50% before it can use prevailing price to value other affiliate transactions. However, 50% is an arbitrary number and far in excess of the amount of outside sales necessary to establish a market rate.

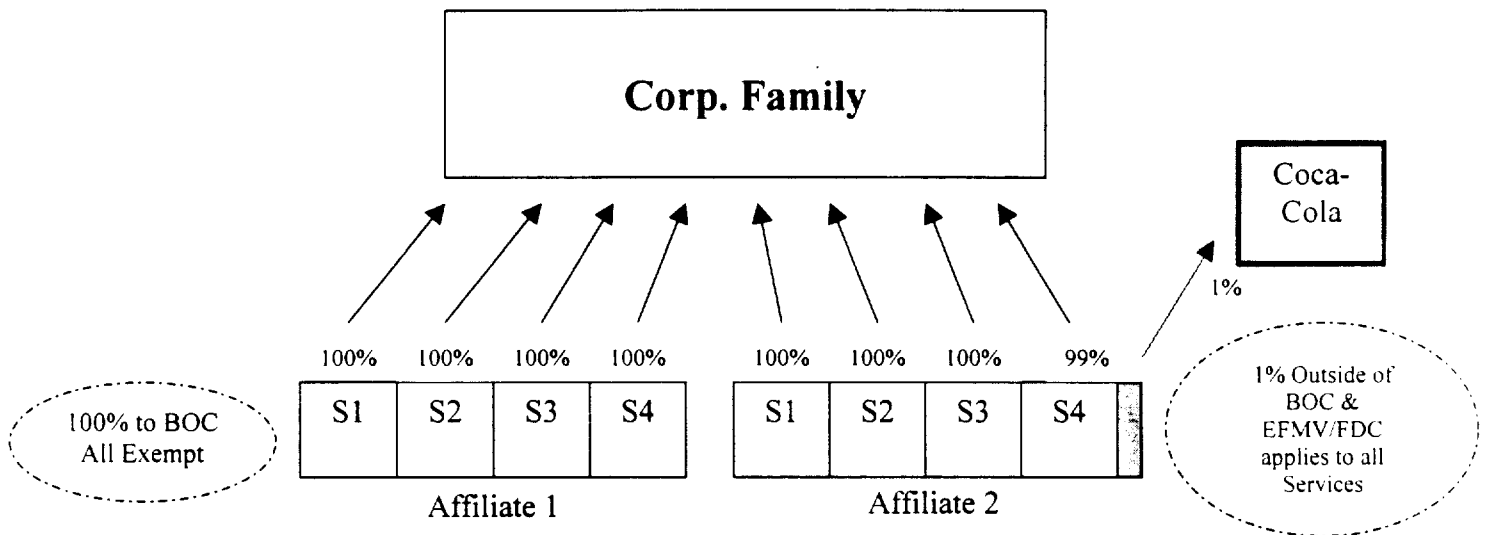
*Solution:* Threshold should be lowered to at least 25%; if 25% of sales for a competitive service are to third parties then clearly a market rate is established.

## Attachment A-1

### Centralized Service Exemption

#### Issue

Current rule exempts services that are received from “affiliate(s) that exist solely to provide services to members of the carrier’s corporate family.” Exemption applies only when entire legal entity provides 100% of all services to corporate family. A single sale of a single service outside the corporate family, triggers EFMV/FDC comparison for all other transactions of that affiliate, even if they are provided 100% w/in family.



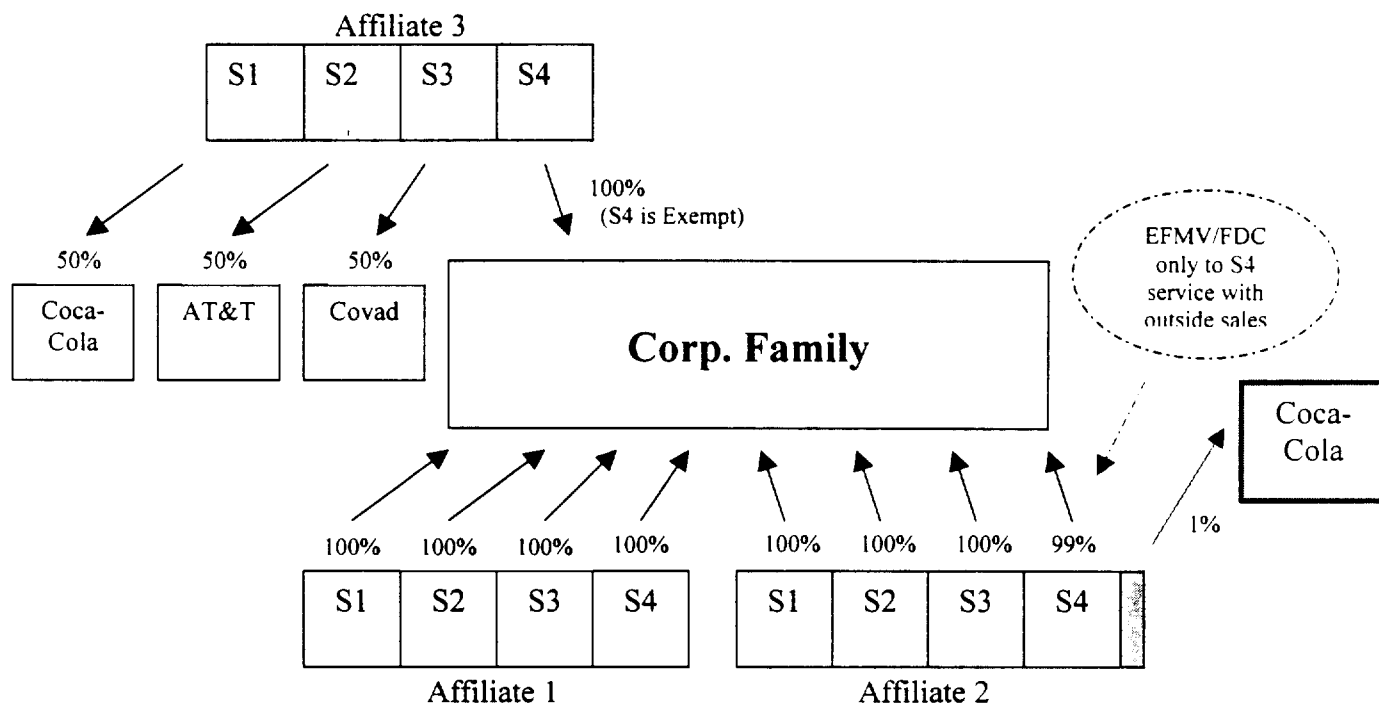
*S=Service*

## Attachment A-2

### Centralized Service Exemption

#### Solution - BLS/USTA Proposal

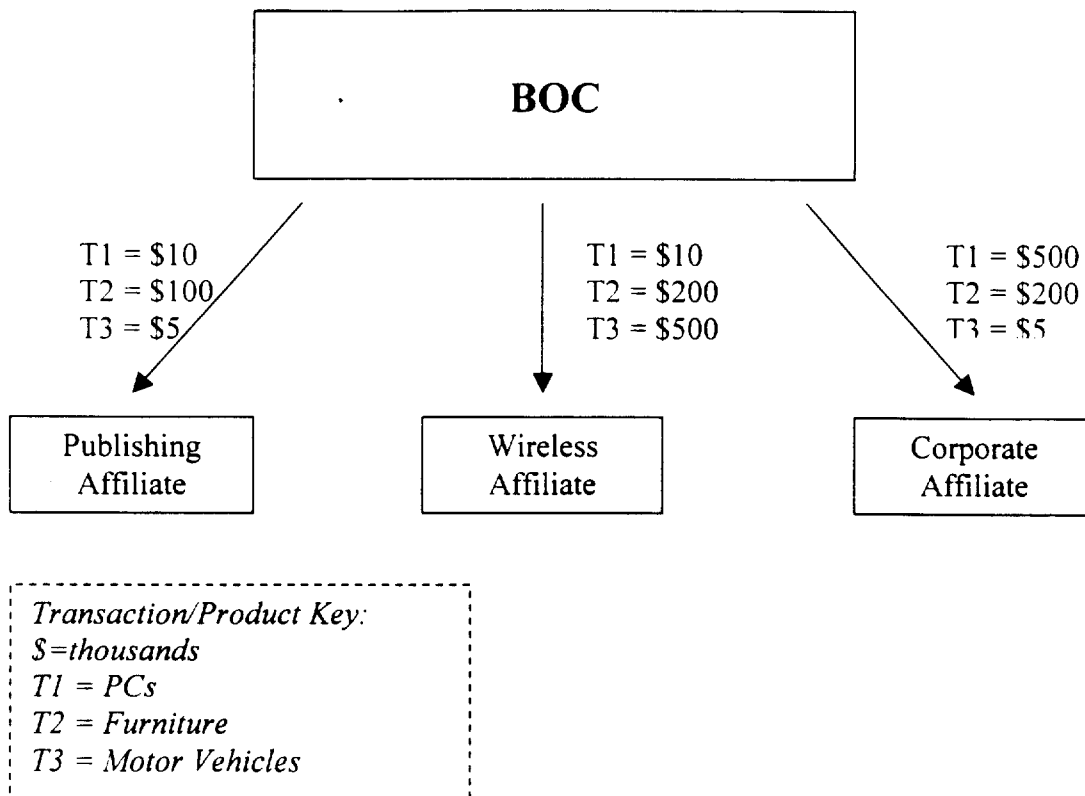
Service exemption should apply on a service-by-service basis instead of being applied to an entire legal entity (i.e., “affiliates that exist solely to service the corporate family.”) There is no benefit gained by limiting the exemption by the status of the affiliate offering the service, only added burden. By applying exemption to any individual service that is provided 100% within the corporate family, relevant transactions will continue to be subject to EFMV/FDC comparison without burdening other services unnecessarily.



#### Impact of adopting BLS/USTA proposal:

- Affiliate 1 = All services would be exempt.
- Affiliate 2 = S1, S2, and S3 would be exempt. S4 subject to EFMV/FDC
- Affiliate 3 = S4 would be exempt; all other services subject to EFMV/FDC.

**Attachment B**  
**Asset Transfer Threshold**



**Issue:**

The Asset Transfer Threshold proposed by the FCC would provide little to no reduction in burden. The diagram, above, represents asset transfer activity.

- Under current rules, *every transaction for every affiliate is subject to the EFMV/FDC comparison.*
- The FCC's proposed \$500,000 threshold would apply on a product-by-product basis for the total amount of transfers for a given product line in a given year. If you add the transactions across affiliates, above, you get the following totals by product line: T1=\$520; T2=\$500; and T3=\$510. Thus, every product line has met the threshold *and the EFMV/FDC would apply to every transaction.*

**Solution:**

The BLS/USTA proposed threshold would apply on a product-by-product, affiliate-by-affiliate basis and would provide significant reduction in burden: *only two transactions* (instead of nine) would be subject to the EFMV/FDC comparison.

- Publishing Affiliate: all product lines remain below threshold.
- Wireless Affiliate: T1 & T2 remain below threshold; product line T3 is \$500 so EFMV/FDC would apply.
- Corporate Affiliate: T1 is \$500 so EFMV/FDC would apply; all others below threshold.

Similarly, FCC's current threshold for service transactions provides almost no reduction in burden. Rule must be modified to apply on affiliate-by-affiliate basis in order to achieve streamlining goals.